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Client Alert

Government Advocacy & Public Policy Practice Group

July 27, 2015

Senate Finance Committee Approves Energy Tax Provisions—LNG Is A Winner

Pathway to Passage

On July 21, the Senate Finance Committee approved by a vote of 23 to 3 a bipartisan tax bill to renew for two years more than 50 expiring and expired tax provisions known as "tax extenders." The provisions that are being extended generally provide tax benefits designed to incentivize particular behavior from American taxpayers, *e.g.*, using renewable energy. As originally enacted, most of these provisions are designed to be temporary incentives and remain in effect for short periods of time, primarily because of their high costs and their impact on the federal budget. Thus, if not "extended" they will permanently expire.

While some would prefer that these provisions either be permanently enacted or otherwise eliminated entirely, in order to provide certainty in the tax code for the next two years and encourage economic growth and development, innovation, and job creation, the Finance Committee once again took this stopgap approach. If approved by Congress, the legislation could cost the federal government an estimated $95 billion over the next 10 years, according to the Joint Committee on Taxation. The Finance Committee has indicated that it will use a broad reform of the tax code in the next few years as a way of determining the long-term fate of these provisions.

Energy Extenders Legislation

Many of the provisions in the extender legislation provide energy-related tax breaks designed to help support American energy jobs, a cleaner environment through renewable energy projects, and energy independence for the United States. For example, the bill would allow renewable energy and energy storage projects to create master limited partnerships, which are businesses organized as partnerships or limited liability companies ("LLCs") and publicly traded, offering capital markets investors the tax benefits of partnerships. The bill also includes a two-year extension of the Production Tax Credit ("PTC") for wind, geothermal, biomass, and landfill gas projects, giving developers an additional two years to begin construction and maintaining the existing option to claim production tax credits or a 30 percent investment tax credit on relevant projects.

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LNG Industry Is A Winner

As a new and important player in the nation's developing domestic energy market, the liquefied natural gas ("LNG") industry is a big winner. Currently, LNG and diesel fuels are taxed at the same 24.3 cent per gallon rate, although a gallon of LNG produces approximately 58 percent of the energy produced by a gallon of diesel fuel. This inequality within the tax system results in thousands of dollars of additional costs for companies that choose to use LNG, despite the fact that LNG produces significantly lower levels of toxic emissions than diesel and reduces pollution from black carbon, a major contributor to climate change. The bill includes a significant tax cut that will equalize the taxation of LNG compared to diesel based on energy production per gallon. The bill changes the tax rate of LNG to a rate based on its energy equivalent of a gallon of diesel fuel (approximately 14.1 cents per gallon) and allows LNG to compete equally with diesel by taxing LNG on energy output rather than on a per gallon basis.

What's Next?

The bill now moves to the Senate floor where it is believed that much of the bill reported out of the Finance Committee will be preserved. Some provisions, however, such as the wind energy production tax credit, are already under attack and may not survive. Whatever passes will be sent to the House, which is considering a different approach.

The House has signaled that it is ready to put an end to the biannual exercise of extending these provisions by deciding to make some of the expired and expiring provisions permanent and allowing others to fall out of the tax code. Accordingly, it is expected to consider a package of permanent tax extenders as part of a broader effort to reform the U.S. tax code when Congress returns from its August recess. According to the Joint Committee on Taxation, making the tax extenders permanent would add more than $1 trillion to the budget deficit by 2025. President Obama has indicated he will veto legislation that makes tax extenders permanent without providing offsets.

Interestingly, the House had already addressed the LNG equalization issue in a separate bill, H.R. 3038, the Highway and Transportation and Funding Act of 2015, Part II. That bill would cut excise fuel taxes on LNG and liquid propane gas ("LPG") used as highway motor fuels. The bill would also tax LNG and propane on an energy-equivalent basis relative to diesel and gasoline, which would lower the taxes paid by these fuels by about $90 million, according to the Joint Committee on Taxation. The package also included a provision that would modify the federal fuel excise tax on LNG and LPG to levels more in line with their energy content. The package adjusts the LNG tax to 14.1 cents per gallon and the LPG tax to 13.2 cents per gallon. So as far as the House is concerned, the industry may get two bites at the apple.

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None of these provisions will be enacted until late fall or early winter. We will monitor this important issue and report as developments unfold. If you would like additional information, please contact us.

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